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IN THE

Supreme Court of the United States

OCTOBER TERM, 1941

No. 286

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner,

v.

SOUTHWEST CONSOLIDATED CORPORATION,
Respondent.

SUPPLEMENT TO BRIEF FOR RESPONDENT

This case involves an old fashioned equity receivership proceeding (R. 32). If the plan were carried out today, in all probability the parties would proceed under Chapter X of the Bankruptcy Act.[1] The tax consequences of a Chapter X proceeding reveal recent[2] Congressional intent as to the tax consequences of insolvency reorganizations.

In his Brief (fn. 2, pp. 7, 8), the Commissioner points out that in a proceeding under Chapter X the debtor's basis, or the basis of "any person required to use the

[1] C. 575, 52 Stat. 840, as amended by c. 500, 54 Stat. 709, Sec. 1.

[2] The Chandler Act was passed in 1938 and amended in 1940.

debtor's basis," shall be decreased by[3] an amount equal to the amount by which the indebtedness of the debtor has been cancelled or reduced in the proceeding, but to an amount not less than fair market value (Sec. 270). This provision is correlative to Section 268 of Chapter X, which provides that the debtor shall not be deemed to have realized income from the reduction of its indebtedness (contrary to such decisions as *United States* v. *Kirby Lumber Company*, 284 U. S. 1).[4]

The provisions for the adjustment of basis in Chapter X are significant here since they recognize that a new corporation created under a Chapter X plan may be required to use the debtor's basis. This is contrary to the Commissioner's primary argument that in an insolvency reorganization basis should not be carried over. It confirms the argument that Congress approved the line of decisions holding an insolvency reorganization within the non-taxable reorganization and basis provisions of the Revenue Act (taxpayer's *Brief*, pp. 10-12). Such decisions as *LeTulle* v. *Scofield*, 308 U. S. 415, and *Helvering* v. *Tyng*, 308 U. S. 527, do not warrant frustration of this legislative intent.

A further guide to the proper decision here is afforded by noting the tax consequences if the present reorganization had been carried out under Chapter X. Assuming no new corporation had been formed, there would be no question as to carry over of basis. However, basis of the old company would have been reduced by an amount equal to the amount by which its indebtedness was reduced

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[3] In his Brief (fn. 2, p. 8) the Commissioner has incorrectly quoted the statute. He quotes it as "decreased to an amount" whereas it should be "decreased by an amount."

[4] H. Rep. No. 1409, 75th Cong., 1st Sess., pp. 55, 56; S. Rep. No. 1916, 75th Cong., 3rd Sess., pp. 7, 8.

(because under Section 268 the old company would not have been taxed on that amount). Where stock is given for indebtedness under a Chapter X plan, the Commissioner considers indebtedness is reduced by the difference, if any, between the fair market value of the stock and the face amount of the indebtedness on account of which the stock is received (G.C.M. 22528, 1941-8 Int. Rev. Bull. 2). In the present case the fair market value of the assets, and hence of the new securities, was $1,766,694.98 (R. 38). The face amount of indebtedness of the old company was $3,029,445.42 (R. 36). The difference is $1,262,750.44. Deducting this amount, pursuant to Section 270 of Chapter X (as interpreted by G.C.M. 22528, *supra*), from the basis of the old company of $8,995,724.91 (R. 38), gives a basis of $7,732,974.47.

If Congress by specific provision saw fit to make adjustments of this nature with such result, it seems clear there was no contemplation by Congress that insolvency reorganizations as such were to be without the non-taxable reorganization and correlative basis provisions of the Revenue Act.

Respectfully submitted,

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January 1942.